

COMMONWEALTH OF KENTUCKY  
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF KENTON COUNTY WATER	)	
DISTRICT NO. 1	)	
(A) TO ISSUE REVENUE BONDS IN THE	)	
APPROXIMATE AMOUNT OF \$21,930,000	)	
(B) TO CONSTRUCT ADDITIONAL PLANT	)	CASE NO. 9846
FACILITIES OF APPROXIMATELY	)	
\$19,214,000; AND	)	
(C) NOTICE OF ADJUSTMENT OF RATES	)	
EFFECTIVE MAY 1, 1987	)	

O R D E R

On March 30, 1987, Kenton County Water District No. 1 ("Kenton County") filed an application seeking authority to construct additional plant facilities, adjust water service rates, and issue revenue bonds in the amount of \$21,930,000. Kenton County proposed an increase in rates to produce additional operating revenue of \$1,748,784. After the adjustments and determination herein, Kenton County is granted authority to increase rates to produce additional operating revenue of \$1,620,370, a 26 percent increase.

A hearing was held in the offices of the Public Service Commission in Frankfort, Kentucky, on July 17, 1987. Taylor Mill Water Commission ("Taylor Mill"), and Kentucky Industrial Utility Customers ("KIUC") previously intervened in this proceeding, but KIUC chose not to participate in the hearing.

As the hearing closed, all participating parties, as well as the Commission staff, were directed to file briefs. In addition,

Kenton County was directed to file certain items of additional information. The briefs and the additional information have been filed and the matter is considered to be fully submitted for final determination by the Commission.

CERTIFICATES OF PUBLIC CONVENIENCE AND NECESSITY

The Commission accepts the staff's recommendation that the proposed construction projects outlined in Exhibit 15 of the application be granted general approval, so that Kenton County may issue securities to fund the proposed projects. In addition, the Commission is of the opinion that the size, complexity, and capital outlay of the several proposed construction projects generally require certificates of public convenience and necessity from this Commission prior to their construction. After reviewing the evidence in this case the Commission does agree with the position taken by Kenton County in its brief of August 18, 1987, that certain of the proposed projects do not require the application for a certificate prior to their construction. The information filed in this case indicates to the Commission's satisfaction that the projects identified in Exhibit 15 as "P. Modify Pumps, T. KY 16 - KY 17 Connector Relocation," and "U. Winston Avenue Relocation" do not fall within the parameters of Commission regulations which require individual certificates of public convenience and necessity. However, the Commission does not concur with Kenton County's contention that the mere fact that construction involves relocation or renovation of existing facilities relieves the utility of the requirement for Commission review and approval.

The Commission was disappointed to discover during the course of this proceeding that two projects labeled A and C on Exhibit 15, totaling over one million dollars, had already been constructed without Commission approval prior to the date of the application in this case. While the Commission will not assess a penalty at this time, future activities of this sort may require the Commission to invoke the penalty provisions of KRS 278.990. The Commission does not certificate construction projects after they have been constructed. No exception will be made in this case. The two projects labeled "A. 36" Transmission Main ..." and "C. 30" Transmission Main ..." on Exhibit 15 will not be certificated by this Commission.

Kenton County concedes in its memorandum brief that none of the remaining construction projects have been sufficiently documented for the granting of a certificate of public convenience and necessity by the Commission at this time. Kenton County proposes that the instant case be left "open" for subsequent information concerning the various construction projects.

To obtain a certificate of public convenience and necessity a utility must petition the Commission and file certain information. These filing requirements are set out in 807 KAR 5:001, Section 8 and Section 9. When this information is completely and timely filed, the Commission's review can be handled expeditiously. In fact, the Commission has, on occasion, been able to review and certificate completely documented construction projects not

requiring rate adjustments in less than 30 days.<sup>1</sup> Unfortunately, the review process is often delayed by an incomplete filing by the utility. In general, a utility should file its application for a certificate prior to advertising for bids on the construction project. With the application the utility should file the following construction-related information:

1. A Preliminary Engineering Report which outlines the necessity of the project, all alternatives considered, construction cost estimates, projected operating cost, design factors used, construction funding, etc.
2. Final Plans and Specifications which detail the proposed construction, prescribe materials to be used and describe construction procedures which must be followed.
3. A Hydraulic Analysis which demonstrates not only the operational characteristics of the proposed addition but also the effect the addition will have on the existing system.
4. Boundary Information - Water Districts must document that the proposed construction is within the boundaries of the District or that the boundaries have been legally expanded to include the new construction area.

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<sup>1</sup> For example, in Case No. 9495, Boone County Water and Sanitation District's application for approval of a construction project, certification was granted 12 days after the filing of the application.

5. All approval documents from other governmental agencies and financing organizations. This would include Division of Water approval, commitment documents from lenders, etc.

After the initial application filing, the utility would be expected to file the following additional documents:

6. A Bid Tabulation which outlines the bids received and identifies those accepted.
7. A Final Engineering Report that is generally a one-page summary outlining the final project estimate based on the bids received and the level of funding. The final project estimate should include construction cost, legal fees, engineering fees, land and right-of-way contingencies, etc. The funding should be broken down into loan funds, grants, applicant contributions, etc. If the project has significantly changed since the preparation of the preliminary Engineering Report, then the necessary revisions should be set out.

In those cases where the construction proposed is routine and no objections are raised, the review process and granting of a certificate can be accomplished without a formal public hearing before the Commission. It is the Commission's opinion that such a process can be effectively utilized by Kenton County for the construction projects proposed in this case.

This Order grants the general approval requested by Kenton County of its construction program, "as a program."<sup>2</sup> Approval of the construction projects proposed but not already completed<sup>3</sup> or otherwise specifically exempted<sup>4</sup> by this Order will be considered when Kenton County supplies the necessary engineering information, previously described in detail by this Order. The Commission will allow Kenton County to avoid repetition by making reference, as necessary, to material already contained in the record of this case, when requests for certificates to construct are filed in the future. Additionally, in order to facilitate the review of the projects that have not been certificated, Kenton County should file remaining construction project details as they become available. Any material filed should clearly identify the project that the material relates to. Such material may be filed with a letter from Kenton County's counsel. After a review, the Commission will determine whether the project should be exempt from certification. If the project is not found to be exempt, a formal case will be opened and docketed. Nothing in this Order should be construed as granting authority for Kenton County to begin the construction of any project not specifically found exempt from certification by this Order.

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<sup>2</sup> Kenton County Brief at page 17.

<sup>3</sup> Projects A and C.

<sup>4</sup> Projects P, T, and U.

Since general approval is being granted by this Order the Commission will, therefore, deny Kenton County's motion for a deviation from the requirements of 807 KAR 5:001(9). Additionally, Kenton County's request for the Commission to leave this case open is denied.

#### BOND ISSUANCE

Since the Commission is not issuing a Certificate of Convenience and Necessity at this time, but is granting approval of the financing plan, Kenton County must adequately plan for any possible decision by the Commission regarding the proposed construction. If a construction project is denied certification by the Commission, the Commission will reduce Kenton County's revenue requirement by the debt service coverage and the depreciation expense associated with the denied project. Therefore, Kenton County should have the necessary provisions in its bond documents that will enable it to act accordingly, in the event that the Commission denies certification of a project or projects.

As stated during the hearing by Terrel Ross of Prescott, Ball, and Turben, a municipal underwriting and investment banking firm, a call provision could be included in the bond documents that would enable the district to recall bonds if a project or projects were denied approval.<sup>5</sup> The Commission is of the opinion that a call provision should be included in the bond documents due to the uncertainty of certification of all the projects.

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<sup>5</sup> Hearing Transcript, pages 68-70.

### TEST-YEAR REVENUES AND EXPENSES

The staff performed a limited review of Kenton County's records for the test-year ending December 31, 1986. As stated in staff testimony filed June 24, 1987, the test-year selected reflects normal operating conditions except for a few minor items. The staff noted that a main line relocation and a population growth study performed during the test-year should be capitalized and amortized over 5 years. Kenton County did not object to this treatment and the Commission is of the opinion that the staff's recommendation should be accepted to reflect normal operating conditions. The net effect of these adjustments, including the related amortization expense, is \$<29,795>.<sup>6</sup>

### PRO FORMA ADJUSTMENTS

Kenton County proposed several pro forma adjustments to revenues and expenses to reflect current and anticipated operating conditions. The staff addressed several of the adjustments in its testimony. The Commission is of the opinion that the proposed adjustments are generally proper and acceptable for rate-making purposes with the following modifications:

### OPERATING REVENUES

In its initial application, Kenton County showed total metered revenues of \$5,732,074 and revenues from forfeited

<sup>6</sup>	Main Line Relocation	\$<19,471>	
	Growth Population Study	<u>&lt;17,773&gt;</u>	\$<37,244>
	Amortization Expense		
	\$37,244 - 5 =		7,449
	Net Adjustment		<u>\$&lt;29,795&gt;</u>



discounts, miscellaneous service, rents from water property and other water revenues of \$103,702, which result in total test year operating revenue of \$5,835,776. Kenton County projected an increase in water sales of 143,900,000 gallons, which increased revenue by \$130,950.

On June 29, 1987, the Commission issued an Order in Case No. 8572<sup>7</sup> granting Kenton County an additional increase in operating revenue as a result of a Franklin Circuit Court decision rendered on February 17, 1987.<sup>8</sup>

On August 4, 1987, Kenton County filed an amended billing analysis which reflected the rate increase granted in Case No. 8572. The revised billing analysis showed metered revenues in the amount of \$5,993,917. The revised increased revenue from the projected increase in water sales of 143,900,000 gallons is \$137,425.<sup>9</sup>

Kenton County projected that its total revenues from forfeited discounts, miscellaneous service, and other water revenues would increase by \$2,244. Kenton County will not receive rent from a portion of its office and shop which results in a decrease in revenue of \$8,000. Based on the aforementioned

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<sup>7</sup> In the Matter of A Rate Adjustment of Kenton County Water District.

<sup>8</sup> Civil Action No. 83-CI-1279.

<sup>9</sup> 
$$\frac{\text{Total Income From Water Sales: } \$5,993,917}{\text{Total Gallons of Water sold: } 6,274,617,100} = \$ .955/1,000 \text{ gallons}$$

1987 Projected Increase in Water Sales:  
 $143,900,000 \text{ Gallons} \times \$ .955/1,000 \text{ gallons} = \$137,425$

adjustments the total revenues to be received from sales, excluding metered revenues, is \$97,946, a decrease of \$5,756.

After adjustments to both the increase in revenue of the projected increase in water sales and the billing analysis as a result of the increase granted in Case No. 8572, and the decrease in other revenues, Kenton County's normalized test year revenues are \$6,229,288.<sup>10</sup>

#### Employee Additions

Kenton County proposed several personnel adjustments totalling \$130,887, per Exhibit 10 of the application. Kenton County proposed to increase the part-time Water Quality Laboratory Analyst position to a full-time position due to the anticipated changes in the Safe Drinking Water Act. Kenton County stated in its Brief filed August 10, 1987, that this position was upgraded to a full-time position in January, 1987, at a net additional annual cost of \$18,690.

Kenton County proposed to add a staff engineer at an additional annual expense of \$15,313. The staff had recommended in its testimony that both the aforementioned pro forma adjustments be excluded from the revenue requirement determination because it was not known when these positions would be filled. Since both positions were filled in January and February, 1987, the Commission is of the opinion that these are known and

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<sup>10</sup> \$5,993,917 Metered Revenues Plus \$137,425  
Projected Increase in Sales Plus \$ 97,946  
Normalized Revenues = \$6,229,288

measurable adjustments and should be included in the revenue requirement determination.

Kenton County also proposed to add two plant operators for the new sludge handling facilities, and to add a laborer to train to replace an employee who will retire in the next year or two. The staff stated in its testimony that the plant operator's adjustment of \$56,053 is premature since the proposed construction will not be completed until April, 1989. The Commission is in agreement with the staff in that the plant operator's adjustment should not be included herein due to the projected completion date, and the resulting mismatch of current revenues and expenses. The Commission is also of the opinion that the proposed laborer adjustment of \$22,111 should not be included since it is not known when the present employee will retire. Therefore, the proposed total adjustment to wages expense of \$130,887 has been reduced by \$78,164.

#### Water Treatment Expenses and Pumping Expenses

Kenton County proposed to include the estimated operation and maintenance costs of the new sludge handling facilities totalling \$32,285. As previously stated, since the completion of the construction is not expected until April, 1989, the Commission is of the opinion that this adjustment is not known and measurable and would not reflect operations during the present and near future periods.

Kenton County also proposed to reduce test-year pumping expense by \$53,228 since, after completion of the proposed construction, three pumping stations will be placed on standby

status. Due to the aforementioned reasons, the test-year pumping expenses have not been reduced.

#### Depreciation Expense

Kenton County reported test-year depreciation expense of \$596,053. Kenton County proposed to increase the test-year expense by \$336,237 due to the proposed construction. Kenton County computed the adjustment using a 1.75 composite depreciation rate. The staff recommended in its testimony dividing the construction projects into three basic categories of transmission mains, 10"-20" mains, and treatment plants, and then utilize Kenton County's actual depreciation rates.

Taylor Mill addressed the issue of excluding any related depreciation expense on assets that are being replaced. Kenton County stated in its response to the hearing data request filed August 4, 1987, that the aggregate annual depreciation expense of the to-be-replaced water lines totals \$506. The Commission is of the opinion that the depreciation expense adjustment should be calculated as described by the staff with an additional adjustment of decreasing the expense by \$506 to reflect the assets which will be replaced. Therefore, the test-year depreciation expense has been increased by \$265,044.<sup>11</sup>

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Assets	Cost	Life	Depreciation Expense
Transmission Mains	\$ 6,779,168	100 yrs.	\$ 67,792
Mains	1,422,284	100 yrs.	14,223
Treatment Plants	11,012,072	60 yrs.	183,535
	\$19,213,524		265,550
			- 506
			<u>\$265,044</u>

#### Annual Repainting of Storage Tanks

Kenton County proposed at the hearing that a pro forma adjustment of \$54,600 should be included in the revenue requirement determination due to the Commission's requirement of having the storage tanks painted. Even though this adjustment was not presented in the application, the expense is known and measurable and, therefore, the Commission has included it herein.

After consideration of the aforementioned adjustments, the Commission finds Kenton County's test year operations to be as follows:

	Test Year Per Exhibit 10	Commission Adjustments	Adjusted Test Year
Operating Revenues	\$5,835,776	\$393,512	\$6,229,288
Operating Expenses	4,410,711	471,021	4,881,732
Net Operating Income	<u>\$1,425,065</u>	<u>\$&lt;77,509&gt;</u>	<u>\$1,347,556</u>

#### REVENUE REQUIREMENTS

Kenton County proposed a Debt Service Coverage ("DSC") of 1.2X on existing and proposed bond issuances. Taylor Mill stated in its brief filed August 24, 1987, that Kenton County has failed to propose an adjustment to its reserve for depreciation for existing plant to account for the replacement of plant by the proposed main line relocations. Taylor Mill did not question Kenton County's proposed 1.2X DSC method, thus making the reserve depreciation issue moot since it is not used in the 1.2X DSC method but in a rate of return on rate base method.

Also, in its brief filed August 24, 1987, Taylor Mill contends that Kenton County has not adequately investigated reimbursement for projects required by state or federal

government. Kenton County stated in its data response to the hearing filed August 4, 1987, that Project U has been designated a Federal Project and Kenton County will be reimbursed \$150,384 of the total estimated project cost of \$179,165. Kenton County further stated that Projects H, I, J, and T will not be reimbursed.

The Commission is of the opinion that Kenton County has adequately pursued the reimbursement matter. However, if Kenton County does receive reimbursement for a project, it should notify the Commission and appropriate rate-making treatment will be pursued.

Kenton County utilized a 6.663 percent interest rate when determining revenue requirements per the application. The Commission is of the opinion that the proposed 6.663 percent interest rate should be utilized herein. However, if at the time of the bond issuance the actual interest rate is materially different, Kenton County should apply for appropriate changes in its rate schedules.

Kenton County requested authority to issue bonds in the approximate amount of \$21,930,000, depending on the actual interest rate at the time of issuance. The Commission is of the opinion that a 1.2X DSC is fair and reasonable and thus has accepted Kenton County's proposed 1.2X DSC of \$4,002,894.<sup>12</sup>

Using a 1.2X DSC plus operating expenses, including the principal and interest payments of \$17,452 on a real estate

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<sup>12</sup> Per Exhibit 13 of the Application.

mortgage, the Commission finds Kenton County's total revenue requirement to be \$8,902,078.<sup>13</sup> After consideration of test-year non-operating income of \$412,306, interest earnings on construction funds of \$640,114, and adjusted operating revenues of \$6,229,288, an increase in annual revenue of \$1,620,370 from water sales will be sufficient.

#### RATE DESIGN

In the instant case, Kenton County did not propose to change the rate structure now in effect. The Commission staff, both in prefiled testimony and testimony at the hearing, recommended that in the absence of a cost of service study it would not be in the best interest of the public nor Kenton County to initiate a new rate design.

In its brief filed August 24, 1987, Taylor Mill stated that it will not benefit from most of the proposed projects. However, Taylor Mill stated that it does not disagree with the staff's position for maintaining the present rate design, but stated that cogent reasons exist for the Commission to consider sub-classes or some other innovative technique to give consideration to Taylor Mill's situation.

While the Commission staff has recommended that a cost of service study is not warranted in this case, the Commission,

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<sup>13</sup>	Adjusted Test-Year Expenses	\$ 4,881,732
	Real Estate Mortgage	17,452
	1.2X DSC	4,002,894
		<u>\$ 8,902,078</u>

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hereby places Kenton County on notice that a cost of service study will be required as part of Kenton County's next rate proceeding.

Based on the evidence of record, the Commission has determined that the rate increase granted herein should be spread to the existing rate structure so that the percentage of revenue from general customers and revenue from water sold for resale remains the same as established in prior cases.

#### CONNECTION FEES

Kenton County provided cost justification to increase its connection fees for a 5/8-inch connection to \$370 and to increase its 1 1/2-inch connection fee to \$700. Kenton County also proposed to increase its connection fee for all sizes greater than a 1-inch connection from actual cost plus 10 percent to actual material costs times 1.1 to cover handling plus actual payroll and equipment costs.

The Commission is of the opinion that the cost justification provided by Kenton County for these services is adequate, and the connection fees proposed by Kenton County should be approved.

#### FINDINGS AND ORDERS

The Commission, after consideration of the evidence of record, and being advised, is of the opinion and finds that:

1. The construction proposed by Kenton County's Exhibit 15 in general is, or will be in the near future, necessary for the provision of adequate and reliable service to the customers of Kenton County and should be granted general approval for financing purposes.



2. The construction proposed by Kenton County as projects P, T, and U in Exhibit 15 do not require certificates of public convenience and necessity prior to construction.

3. Kenton County's motion for a deviation from the requirements of 807 KAR 5:001, Section 9, should be denied.

4. Kenton County's request to leave Case No. 9846 open should be denied.

5. Kenton County should furnish duly certified documentation of the total costs of projects A and C of Exhibit 15 including the cost of construction and all other capitalized costs (engineering, legal, administrative, etc.). Said construction costs should be classified into appropriate plant accounts in accordance with the Uniform System of Accounts for Water Utilities prescribed by the Commission.

6. Kenton County should furnish a copy of the "as-built" drawings for projects A and C of Exhibit 15 and a signed statement from the Engineer that the construction has been satisfactorily completed in accordance with the contract plans and specifications.

7. The rates proposed by Kenton County would produce revenue in excess of that found reasonable herein and, therefore, should be denied upon application of KRS 278.030.

8. The rates in Appendix A are the fair, just, and reasonable rates for Kenton County in that they are calculated to produce gross annual revenue from water sales of \$7,751,712. These revenues will be sufficient to meet Kenton County's

operating expenses found reasonable for rate-making purposes, service its debt, and provide a reasonable surplus.

9. The approximate \$21,930,000 bond issuance proposed by Kenton County is for lawful objects within its corporate purposes and is necessary or appropriate for or consistent with the proper performance of its services to the public and will not impair its ability to perform these services, and is reasonably necessary and appropriate for such purposes, and should, therefore, be approved.

10. The cost justification provided by Kenton County for its proposed increase in connection fees is adequate and the proposed fees should be approved.

IT IS THEREFORE ORDERED that:

1. Kenton County's proposed construction be and hereby is granted general approval for financing purposes.

2. Kenton County's position that projects P, T, and U in Exhibit 15 do not require a certificate be and hereby is affirmed.

3. Kenton County's motion for a deviation from the requirements of 807 KAR 5:001, Section 9, be and it hereby is denied.

4. Kenton County's request to leave Case No. 9846 open be and it hereby is denied.

5. Kenton County shall comply with all matters set out in Findings 5 and 6 as if the same were individually so ordered.

6. Nothing in this Order shall be construed as granting authority for Kenton County to begin the construction of any project not specifically found exempt from certification by this Order.

7. The rates proposed by Kenton County are hereby denied.

8. The rates and charges in Appendix A are approved for services rendered by Kenton County on and after October 1, 1987.

9. Kenton County's proposed bond issuance of approximately \$21,930,000 is hereby approved.

10. Pursuant to KRS 278.300(4), securities issued pursuant to this Order, or proceeds of such securities, shall be used for the lawful purposes specified in the application.

11. If the actual interest rate at the time of bond issuance is materially different than the one used in the application, Kenton County shall apply for appropriate changes in its rates.

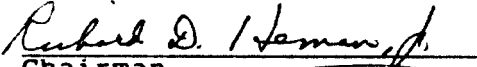
12. The connection fees proposed by Kenton County be and they hereby are approved.

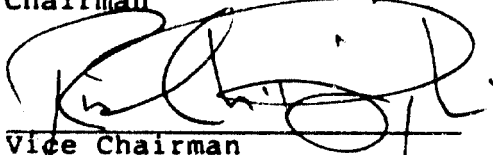
13. Within 30 days from the date of this Order, Kenton County shall file its revised tariff sheets setting out the rates approved herein.

14. Nothing contained herein shall be deemed a finding of value for any purpose whatsoever, nor construed as a warranty by the Commonwealth of Kentucky or any agency thereof as to the securities authorized herein.

Done at Frankfort, Kentucky, this 7th day of October, 1987.

PUBLIC SERVICE COMMISSION

  
Chairman

  
Vice Chairman

  
Commissioner

ATTEST:

\_\_\_\_\_  
Executive Director

## APPENDIX A

### APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE COMMISSION IN CASE NO. 9846 DATED 10/07/87

The following rates and charges are prescribed for the customers in the area served by Kenton County Water District. All other rates and charges not specifically mentioned herein shall remain the same as those in effect under authority of this Commission prior to the effective date of this Order.

#### General Service Area

#### Quarterly Rate

First	600 cubic feet	\$7.86 Minimum Bill
Next	4,400 cubic feet	1.12 per 100 cubic feet
Next	495,000 cubic feet	.97 per 100 cubic feet
Next	1,500,000 cubic feet	.79 per 100 cubic feet
Over	2,000,000 cubic feet	.58 per 100 cubic feet

#### Wholesale Rates

The City of Florence, Kentucky, Boone County Water District, the City of Independence, Kentucky, Taylor Mill Water commission, and the City of Walton, shall be charged the following rate:

All Water Purchased	\$0.62 per 100 cubic feet
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The City of Bromley, Kentucky, the City Ludlow, Kentucky, Campbell County Water District, the City of Wilder, Kentucky, and the Winston Park Water Department, shall be charged the following rate:

All Water Purchased	\$0.58 per 100 cubic feet
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#### Connection Fees

5/8-inch connection	\$370.00
1-inch connection	700.00

All service installation over 1-inch will be charged actual material costs (times 1.1 to cover handling) plus actual payroll costs and equipment costs.